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IN THE
Supreme Court of the United States
OCTOBER TERM, 1988

MEDICAL MALPRACTICE INSURANCE ASSOCIATION,
Petitioner,
v.
SUPERINTENDENT OF INSURANCE OF THE STATE OF NEW YORK,
Respondent.

On Petition for a Writ of Certiorari to the Court of Appeals of the State of New York

BRIEF OF AMICUS CURIAE AMERICAN INSURANCE ASSOCIATION IN SUPPORT OF PETITIONER

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BRIEF OF AMICUS CURIAE AMERICAN INSURANCE ASSOCIATION IN SUPPORT OF PETITIONER

INTEREST OF AMICUS

The American Insurance Association ("AIA") is a national trade organization representing 204 companies writing property/casualty insurance in every State and jurisdiction of the United States. Together, these companies write more than twenty-seven percent of the total property/casualty premiums written annually and represent over twenty-seven percent of the industry's assets. AIA member companies write over twenty-six percent of the Nation's medical professional liability insurance, the insurance that enables American physicians to safeguard the Nation's health. In addition, AIA member companies employ 130,000 people and are affiliated with 65,000 independent insurance agents nationwide. A substantial number of AIA members are also members of petitioner Medical Malpractice Insurance Association ("MMIA"), and three currently serve on MMIA's board of directors.

AIA's purposes are to promote the legislative and public standing of its members and the insurance industry; to provide a forum for discussion of issues that are of common concern to the property/casualty insurance industry; to keep members informed of regulatory and legislative developments; and to serve the public interest through appropriate activities including the promotion of safety and security of persons and property.

The decision of the New York Court of Appeals in this case is wrong and unfair. Unless corrected, it will have substantial adverse consequences for members of MMIA and, as set forth in Section III of this brief, for the insurance industry and its customers nationwide. AIA is uniquely situated to advise the Court about these far-reaching consequences of the Court of Appeals' decision.

The parties have consented to the filing of this *amicus* brief. Their letters of consent are on file with the Clerk of this Court.

INTRODUCTION

The Court of Appeals has issued an extraordinary ruling, to the effect that the State of New York may 1) create a private entity; 2) compel other private entities to financially support it; and 3) then compel it indefinitely to subsidize a particular class of New York citizens. The Court of Appeals does so by proclaiming, first, that the state-created, privately funded and privately directed entity has no federal rights; and second, that the forced subsidization is legitimate because the State *may*, at some future point, permit the entity to recoup its losses over—at *best*—the course of fifteen years.

Both the Superintendent of Insurance and the Court of Appeals conceded below that the rates set by the Superintendent for the 1985-1988 policy years of petitioner MMIA are inadequate to maintain MMIA solvency unless one considers as "present income" the proceeds of a hypothetical future surcharge that *might* permit MMIA to recoup the losses by the turn of the century at the earliest.

Three important issues of Federal law are therefore presented:

1. May a State create an independent legal entity, compel private corporations to support and operate it, confer on it the rights to own property and to contract, and then cause it to incur large deficits without regard to the constraints of the Fourteenth Amendment?

2. May a State justify an otherwise confiscatory and unconstitutional rate on the theory that it may possibly permit imposition of a surcharge on future rates to recoup the loss?

3. Even assuming it may consider a possible future surcharge in setting present rates, may a State

impose a rate structure that concededly requires the regulated business to operate at a deficit for at least fifteen years?

These legal issues have national importance. The bill for MMIA's huge deficits must, according to statute, be paid by the private insurance companies who are compelled to support MMIA financially, an enormous economic burden for which, in justice, they should not be held responsible. The rules established by the Court of Appeals permit any State, without constitutional limitation, to compel selected companies or individuals to subsidize particular classes of state citizens. Because New York is a bellweather State in the insurance industry, this decision will very likely spawn similar actions with respect to medical malpractice joint underwriting associations ("JUA's") in other States. It gives legitimacy to parochial political pressure to set inadequate rates which impose the costs of expensive services on the national companies that provide those services. And States may create similar schemes to compel private subsidies in other areas of insurance or in other regulated industries. Review is therefore urgently needed.

ARGUMENT

I. The Court of Appeals Incorrectly Held That The State May Compel Private Businesses To Act As Sureties For A State-Created Entity, And Then Confiscate That Entity's Property Without Any Federal Constitutional Constraint.

New York law compels all insurance companies directly writing personal injury liability insurance in the State to be "members" of MMIA, a medical malpractice JUA. N.Y. Ins. Law § 5502(a) (McKinney 1985).[1] It requires assessment of member companies for deficits arising from operations. N.Y. Ins. Law §§ 5503(b), 5507(b)

[1] MMIA's private insurer members elect a majority of MMIA's board of directors, and thus effectively control MMIA's operations. *See* N.Y. Ins. Law § 5508(a) (McKinney 1985).

(McKinney 1985). Although the State created MMIA, and compels private insurers to participate in and underwrite it, New York provides no state funds to support MMIA. New York law compels MMIA to offer substantial medical malpractice insurance coverage[2] upon application by any licensed physician or surgeon, N.Y. Ins. Law §§ 5502(e), 5506 (McKinney 1985 & Supp. 1989); N.Y. Comp. Codes R. & Regs. tit. 11, 70.9(c)(1) (1988) (Twelfth Amendment), yet through rate regulation New York has persistently refused to permit MMIA to charge premiums adequate to offset the liabilities the State compels MMIA to assume. As a result, the State has caused MMIA to incur huge deficits, for which its members are liable, that as of the end of 1985 totalled $80-$85 million on a fully discounted basis.[3] Thus, thanks to inadequate rates, MMIA's members are responsible to underwrite an enormous debt.

By statute, MMIA is a legal entity, separate and distinct from its members. N.Y. Ins. Law § 5502(b) (McKinney 1985). New York law confers on MMIA the power to contract and own property, N.Y. Ins. Law § 5502(b), (e) (McKinney 1985 & Supp. 1989), and, of course, to sue and be sued in its own name.[4]

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[2] Each applicant is "entitled to purchase a policy providing primary limits not to exceed one million dollars for each claimant and three million dollars for all claimants in any one year." MMIA must also offer excess coverage. N.Y. Ins. Law § 5502(e)(1) (McKinney 1985 and Supp. 1989).

[3] According to one study, as of the end of 1987, MMIA's deficit had reached $244,800,000 on a fully discounted basis. R. Kenney, National Coordinating Committee on Medical Malpractice JUAs, 1987 Finanical Condition of Medical Malpractice JUAs at i ("NCC Study"). The Study concluded that MMIA's financial condition is "rapidly deteriorating." *Id.* at ii. *See id.* at 15.

[4] The power to be sued is implicit in the power to enter into contracts of insurance. MMIA maintained the present suit in its own name without any question being raised by the state Attorney General or the New York courts about MMIA's power to do so.

Despite these powers, the Court of Appeals inexplicably ruled that MMIA *has no federal rights* because as "a creature of statute . . . all of [MMIA's] rights, obligations and duties have been defined by the Legislature." *In the Matter of Medical Malpractice Insurance Ass'n v. Superintendent of Insurance*, Cert. Petition, App. A, at 12a-13a (*"MMIA v. Sup't"*). The holding is utterly untenable. This Court has consistently rejected the notion that a State may take away property interests it has created without regard to the procedural and substantive commands of the Due Process and Takings Clauses. The Court has recognized that this theory, that property owners must accept the "bitter with the sweet," would effectively undermine *all* constitutional protection for private property. *See Cleveland Bd. of Educ. v. Loudermill*, 470 U.S. 532, 540-41 (1985) ("the 'bitter with the sweet' approach misconceives the constitutional guarantee. . . . The right to due process 'is conferred, not by legislative grace, but by constitutional guarantee.' "); *Webb's Fabulous Pharmacies, Inc. v. Beckwith*, 449 U.S. 155, 163-64 (1980) (rejecting State's claim that because it required private entities to contribute to a fund, State was entitled to the interest earned by the fund; "a State, by *ipse dixit*, may not transform private property into public property without compensation"). Having recognized that MMIA has traditional property rights such as the right to own property and to contract, the State simply may not appropriate MMIA's property without compensation, or without affording due process,[5]

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[5] This Court's decision in *Webb's Fabulous Pharmacies* precludes the Court of Appeals' holding in the instant case. There, the State required certain private parties to an interpleader action to pay funds into court for eventual distribution to the funds' rightful, and as yet undetermined, owner. By statute, the State provided that the interest earned by the fund, while held by the court, belonged to the State. Once deposited, the funds were considered "public money," and the Florida courts upheld the statute on the theory—indistinguishable from the New York court's theory here—that "the statute takes only what it creates": under state law the fund belonged to the State, not any private party. *Webb's Fabulous*

on the theory that this privately supported and operated association was "a statutory entity created by the legislature." *MMIA v. Sup't*, Cert. Petition at 13a.

To the contrary, in 1987, this Court made clear that an entity chartered by Congress is *not* a government agent, but a private actor. *San Francisco Arts & Athletics v. Olympic Comm.*, 107 S. Ct. 2971, 2985 (1987). The Court observed that "[a]*ll* corporations act under charters granted by a government, usually a State. They do not thereby lose their essentially private character." *Id.* (emphasis added). Nor, therefore, do they lose their constitutional rights. *See generally First National Bank of Boston v. Bellotti*, 435 U.S. 765, 778-80 n. 14 (1978).[6]

Pharmacies, 449 U.S. at 158-59. This Court struck down the State's appropriation of the interest on this fund, holding that a State may *not* define away the customary, constitutionally protected incidents of property ownership, which are protected from confiscation by the Takings Clause. *Id.* at 164.

[6] The cases relied upon by the Court of Appeals stand for the opposite propositions from those for which they were cited. In *Brooks-Scanlon Co. v. Railroad Comm'n*, 251 U.S. 396 (1920), this Court articulated the special rule, irrelevant here, that where an entity *contracts* in its charter to do an act, as long as it chooses to operate under the charter it can be held to that commitment notwithstanding the fact that it later proves impossible to perform it at a profit. *Id.* at 399. But Brooks-Scanlon made clear that the imposition of rate-ceilings that guaranteed that the entity would sustain a loss was unconstitutional: "[a] carrier cannot be compelled to carry on even a branch of business at a loss, much less the whole business of carriage. . . . The plaintiff [cannot] be compelled . . . to maintain a railroad for the benefit of others who do not care to pay for it." *Id.* And in *Missouri Pacific R.R. Co. v. Kansas*, 216 U.S. 262, 278 (1910), and *Atlantic Coast Line R.R. Co. v. North Carolina Corp. Comm'n*, 206 U.S. 1, 26 (1907), this Court clearly distinguished between a contractual duty to perform an obligation even if no profit can be realized as a practical matter —which may be enforced without offending Due Process—and rate regulation that on its face denies just and proper remuneration. Because the instant case involves a legislative scheme that compels MMIA to write insurance and fixes rates that concededly impose a substantial deficit, each of the cases relied upon by the court below actually undercut its holding.

Similarly, despite the Court of Appeals' suggestion it is irrelevant that "MMIA is a nonprofit unincorporated association." *MMIA v. Sup't*, Cert. Petition at 13a. Nonprofit entities, *see, e.g., Riley v. National Federation of the Blind*, 108 S. Ct. 2667 (1988) (permitting constitutional challenge by non-profit groups); *FEC v. Massachusetts Citizens for Life*, 107 S. Ct. 616 (1986) (same), and unincorporated associations, *see, e.g., California State Auto. Ass'n Inter-Insurance Bureau v. Maloney*, 341 U.S. 105, 108 (1951) (due process challenge by unincorporated insurance association); *Help Hoboken Housing v. City of Hoboken*, 650 F. Supp. 793, 795 (D.N.J. 1986) (takings clause challenge by unincorporated association), possess constitutional rights including the rights to due process of law.

Nor is MMIA deprived of constitutional rights because it is highly regulated. *Compare MMIA v. Sup't*, Cert. Petition at 12a-13a. It is well-established that the power to regulate even a highly regulated industry does *not* confer the power to disregard the Due Process or Takings Clauses. *See Duquesne Light Co. v. Barasch*, 109 S. Ct. 609, 615 (1989); *Consolidated Edison Co. v. Public Service Comm'n*, 447 U.S. 530, 535, n. 1 (1980); *Atlantic Coast Line R.R. Co. v. North Carolina Corp. Comm'n*, 206 U.S. 1, 20 (1910). As recently as January, this Court made clear that a public utility, whose "assets are employed in the public interest," is protected by the Constitution "from being limited to a charge for [its] property serving the public which is so 'unjust' as to be confiscatory.'" *Duquesne Light Co. v. Barasch*, 109 S. Ct. at 615.

At bottom, the Court of Appeals' decision was a transparent, result-oriented attempt to avoid ruling on the due process issue presented: whether the Superintendent's deliberate setting of rates inadequate to maintain MMIA's solvency was "confiscatory" as a matter of federal law. Its ruling would permit States to confiscate the property of all state-created and state-regulated private entities at will.

II. This Case Squarely Presents An Important Issue Of Federal Law Left Open In *Duquesne Light Co. v. Barasch:* Does The Fourteenth Amendment Prohibit The State From Setting Rates Even It Must Concede Render A Regulated Entity Insolvent, On The Theory That The State *May,* In Subsequent Years, Institute A Compensatory Rate Increase.

In *Duquesne Light Co. v. Barasch,* 109 S. Ct. 609 (1989), this Court ruled that although no particular *method* of rate-making is constitutionally required, rate-making with a confiscatory *impact* is unconstitutional. *Id.* at 617-619; *id.* at 620 (Scalia, J., concurring, joined by Justices White and O'Connor). As Justice Scalia observed, "the Constitution . . . looks to the *consequences* a governmental authority produces rather than the techniques it employs." *Id.* (emphasis added). *This* case squarely presents a challenge to the *consequences* of New York's rate-regulation: the State *admits* that the rates it imposed are inadequate to maintain MMIA's solvency. The issue presented is whether New York may do so on the theory that sometime in the *future* it may—but is not obligated to—authorize a surcharge sufficient to recoup losses sustained by MMIA under the present rates.

The parties are in agreement that "without . . . consideration of future surcharges," the rates set for MMIA by the Superintendent for policy years 1985-1988 "are entirely inadequate to meet the statutory standards of solvency under the Insurance Law." *MMIA v. Sup't,* Cert. Petition at 5a.[7] The Court of Appeals agreed, *id.,* holding that New York law *requires* the Superintendent to consider these merely *possible* future surcharges as if they were presently "income earned," *id.* at 8a, thereby assuring that present rates will be inadequate to cover liabilities presently assumed.

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[7] New York insurance law defines insolvency in relevant part as inability "to pay . . . outstanding lawful obligations as they mature in the regular course of business, as shown by an excess of required reserves and other liabilities over admitted assets." N.Y. Ins. Law § 1309(a) (McKinney 1985).

It is indisputable there can be no guarantee the Superintendent will authorize adequate future surcharges; indeed they may well prove to be illusory.[8] The Court of Appeals conceded that the present rates were based only on "the *assumption*" of "the Superintendent's *willingness* to permit 'adequate' increases beginning in 1988-1989 and the following years." *Id.* at 10a (emphasis added).

The Court of Appeals further conceded that—even assuming substantial future "surcharges" would be put into effect —"MMIA may well be forced to run at a deficit until the surcharges result in recoupment in approximately the year 2000." *Id.* at 11a. Thus, even if the Superintendent and the state legislature find the will to permit MMIA to charge the substantially above-cost (up to 25%) future surcharges counted as "present income" by the Superintendent when calculating the 1985-1988 rates, it is uncontested in this record that MMIA will be forced to carry liabilities for policy years 1985-1988 significantly in excess of its assets *for more than a decade.* See *id.* at 10a. Because the Superintendent has not shown any inclination to allow MMIA to charge rates adequate to offset liabilities currently incurred—much less rates twenty-five percent above that level—it is clear that New York

---

[8] The statute as most recently amended provides that "the Superintendent shall impose a surcharge on premiums" to recoup a projected deficit. But the statute makes clear that the Superintendent's action may take place sometime "on *or after*" July 1, 1989, not to *exceed* eight percent of the established rate until July 1, 1991, "at which time and thereafter such surcharge shall not *exceed* twenty-five percent" of the approved rate. N.Y. Laws. ch. 186, § 1 (McKinney 1988) (emphasis added). The law sets no time-table within which deficits must be recouped. Thus, although arguably the Superintendent must institute *some* surcharge at *some* time, apparently he may institute it whenever he wishes, and may set it at a level down to 1 percent or lower in his sole discretion. Furthermore, the surcharge would be expressed as a percentage of rates in future premium-years, and its effectiveness in recouping prior deficits would plainly turn on whether those future rates were themselves adequate to offset the liabilities assumed in each future premium-year. An adequate surcharge can therefore be seen only as merely *possible* at best.

may *never* permit MMIA to charge a rate sufficient to meet the liabilities it is statutorily compelled to assume.[9] Moreover, even if the Superintendent permits a facially adequate surcharge, there is no guarantee it will be effective; many doctors faced with a choice of paying rates twenty-five percent above adequate levels or self-insuring or seeking alternative risk-spreading devices will almost certainly stop purchasing insurance subject to the surcharge. Without customers willing to pay rates bloated by the surcharge, the authority to include a surcharge in future rates may be of no value to MMIA. Thus, there is substantial doubt that New York will ever truly permit MMIA to recoup the losses it has been forced to sustain in the period at issue.

In the insurance industry, as in all others, it is essential that rates be sufficient to offset the costs of providing the product at issue. An insurance company's "product" is the assumption of the customer's potential liabilities during the term of coverage. Responsible pricing of the insurance product ensures that current assets and anticipated earnings thereon will offset the projected liabilities assumed based upon actuarially sound predictions. *See, e.g.*, R. Mehr & E. Cammack, Principles of Insurance

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[9] Indeed, the Court of Appeals' hypothetical future surcharge theory would permit the State to play an escalating deficit "shell game" with devastating results. The New York Insurance Department in a recent statutorily-mandated report to the Governor and Legislature conceded that MMIA has been compelled to charge inadequate rates in every year of its existence. N.Y. Ins. Dept., *A Balanced Prescription for Change: Report of the New York State Insurance Department on Medical Malpractice* 73-74 (1988). Nothing would stop the Superintendent from authorizing a surcharge on inadequate future rates, thereby perpetuating the deficit. Any surcharge applied to inadequate rates will not return sufficient capital to eradicate MMIA's enormous 1985-88 deficit even by the year 2000. Moreover, the Superintendent could designate 25% of an inadequate future rate as a "surcharge"—thereby allegedly "recouping" past deficits while generating truly staggering *future* deficits. The possibility the State could play this "shell game" until MMIA collapses highlights the absurdity of permitting rates to be set on the basis of hypothetical future "surcharges."

789-90 (1967); C. Kulp & J. Hall, Casualty Insurance 772-76 (1968). If they are not, a company will become insolvent, even if there is sufficient cash-flow to pay claims that come due today. *See* N.Y. Ins. Law § 1309 (McKinney 1985). Adequate rates (those that maintain solvency) are essential to avoid insurance company failure when the assumed liabilities mature. R. Mehr & E. Cammack, *supra*, at 789.

New York's insistence that MMIA charge rates that do not maintain solvency poses two important questions about constitutional limits on rate-making: *First*, may the State fix rate-ceilings that concededly prevent a company from retaining assets sufficient to offset liabilities the State compels it to assume on the theory that the State *might*, at some future time, permit the company to charge a substantially higher price? *Second*, may the State fix rate-ceilings that—even under the rosiest of scenarios—will require the company to wait more than a decade to recoup the deficits thereby imposed? These important issues are squarely within the zone of legitimate constitutional challenges to rates identified in *Duquesne Light*—challenges to the confiscatory *impact* of state-set rates.

As to both questions, the Court of Appeals' decision was radically at variance with principles announced in this Court's precedents and the decisions of lower courts. This Court has repeatedly held that if a State chooses to fix the rates at which private entities may offer their services, those rates must be just and reasonable, and cannot be set so low as to be confiscatory. *Id.* at 615; *Federal Power Comm'n v. Texaco, Inc.*, 417 U.S. 380, 391-92 (1974); *Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591, 602 (1944). And although the determination of what is a "fair rate of return" may vary from case to case depending upon "the risks under a particular rate-setting system, and on the amount of capital upon which the investors are entitled to earn that return," *Duquesne Light Co.*, 109 S. Ct. at 617, in *no* case

can it be "reasonable" or "just," *see id.*, to fix a rate that mandates operation at a deficit for a prolonged period of time.[10] In *Hope Natural Gas Co.*, this Court made clear that a state-set rate is confiscatory if its "total effect" fails to return "not only . . . operating expenses but also . . . the capital costs of the business." 320 U.S. at 602-603. Indeed, no more straightforward definition of a "confiscatory" rate could be advanced than one that compels the seller to take less in payment than his cost for the product.

Use of a merely possible—perhaps even nonexistent—future price increase to justify rates that are otherwise presently confiscatory violates the most basic tenets of due process. As long ago as 1935, Justice Cardozo made clear that "[p]resent confiscation is not atoned for by merely holding out hope of a better life to come." *West Ohio Gas Co. v. Public Utilities Comm'n*, 294 U.S. 79, 83 (1935). Similarly, in *Mora v. Mejias*, the First Circuit rejected the notion that the State may fix a price-ceiling

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[10] *See Mora v. Mejias*, 223 F.2d 814, 818 (1st Cir. 1955) ("it is well settled that it is a deprivation of property without due process of law for a state to compel a public utility to continue to operate at a loss"); *Aetna Casualty & Surety Co. v. Commissioner*, 358 Mass. 272, 281, 263 N.E.2d 698, 703 (1970) (State "may not constitutionally fix rates which are so low that if insurers engage in business they may do so only at a loss"); *Jordan v. American Eagle Fire Ins. Co.*, 169 F.2d 281, 289 (D.C. Cir. 1948) (insurance rates must be set so as to provide "enough revenues for operating expenses, capital costs, and sufficient return to the equity owner to assure financial integrity of the enterprise, so as to maintain its credit and to attract capital"), *citing Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591 (1944); *Isla Petroleum Corp. v. Department of Consumer Affairs*, 640 F. Supp. 474 (D.P.R. 1986) (holding unconstitutional certain rates because the "scene is set to force the plaintiffs to operate losing money until the defendant evaluates the matter later this year"), *aff'd on other grounds*, 811 F.2d 1511 (Temp. Em. Ct. 1986), *rev'd on other grounds*, 108 S.Ct. 1350 (1988); *Brooks-Scanlon Co. v. Railroad Comm'n*, 251 U.S. at 399 ("[a] carrier cannot be compelled to carry on even a branch of business at a loss, much less the whole business of carriage").

that requires a regulated entity to sustain a present loss on the theory that the costs of providing the product *might* later diminish, thereby permitting the entity to recoup its losses. 223 F.2d at 819. A rule permitting presently confiscatory rates based on a mere possibility of future recoupment would give States *carte blanche* to impose losses on rate-regulated industries, thereby forcing them to subsidize their customers. *See generally id.* at 818 (it is unconstitutional for government to "deliberately set out to subsidize . . . consumers at the expense" of the regulated entity). *Any* price—even a forced giveaway—could be justified on the theory that the State *might* someday authorize a huge price increase.[11]

Moreover, New York's actions here are insupportable even if the State *may* in theory rely upon its possible future surcharges to justify present rates. By the Court of Appeals' and the Superintendent's own concession, under the most optimistic scenario considered when these rates were set, "the deficit caused by the 1985-1988 rates could be cured by approximately the year 2000." *MMIA v. Sup't*, Cert. Petition at 10a; *see id.* at 11a. It has long been established that compelled operation at a deficit for any significant period of time is a confiscatory violation of due process. No court of which *amicus* is aware has sanctioned a period of mandated losses even close to the twelve to fifteen years contemplated here.[12]

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[11] The Superintendent's rosy conjectures about the possible effects of tort reform on the projected deficits are similarly insufficient to justify rates that are presently confiscatory. *See West Ohio Gas Co. v. Public Utilities Co.*, 294 U.S. at 83; *Mora v. Mejias*, 223 F.2d at 819.

[12] *See, e.g., Newton v. Consolidated Gas Co. of New York*, 258 U.S. 165, 175 (1922) (holding that company was entitled to relief where the prescribed rate had yielded no fair return for more than a year); *Smith v. Illinois Bell Telephone Co.*, 270 U.S. 587, 591 (1926) ("[p]roperty may be as effectively taken by long-continued and unreasonable delay in putting an end to confiscatory rates as by an express affirmance of them"; lack of action for five years was unconstitutional taking); *Bluefield Improvement Co. v. Public*

This matter therefore offers an important opportunity for this Court to give content to the as-yet undefined constitutional "margins" of state rate-setting authority alluded to in *Duquesne Light*. *See* 109 S.Ct. at 617.

III. The Court Of Appeals' Decision Is Unfair And Dangerous; It Invites States To Solve Fiscal And Policy Problems By Shifting The Cost Of Liability Insurance From The Beneficiary Or The State, Where It Properly Belongs, To The Insurer.

"It is axiomatic that the Fifth Amendment's just compensation provision is 'designed to bar Government from forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole.'" *Pennell v. City of San Jose*, 108 S. Ct. 849, 856 (1988) (citation omitted). New York's actions in this case, initiated by its legislature and carried out by its Superintendent and Court of Appeals, are designed to force insurers to underwrite the cost of medical malpractice insurance, thereby solving two public problems for which those insurers are in no sense responsible: the

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Service Comm'n, 262 U.S. 679, 690 (1922) ("Rates which are not sufficient to yield a reasonable return on the value of the property used at the time it is being used to render the service are unjust, unreasonable, and confiscatory, and their enforcement deprives the public utility company of its property in violation of the Fourteenth Amendment."); *Prendergast v. New York Tel.*, 262 U.S. 43, 49 (1922) (deprivation of fair rate of return for seven months held confiscatory).

In *Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591 (1944), this Court abandoned the detailed review of *methodology* involved in the early rate-setting cases. But this Court has never abandoned the principle—implicit in the Takings and Due Process Clauses—that there is some price below which the State may not compel a merchant to sell. *Id.* at 603. Nor has the Court abandoned the propositions, implicit in this concept, that a rate-setting board may not ask a seller to look to the sale of future products to offset mandated present sales at confiscatory rates, or that a business cannot be forced to wait an extended period of time before it may charge rates that permit it to break even.

fiscal crisis in which most governments—federal, state, and local—presently find themselves, and the high costs imposed on society by medical malpractice. The former is the result of excess government spending or insufficient taxation for which the legislature itself is responsible. The latter is the result of the number and severity of the medical malpractice actions filed against physicians, hospitals and other health care providers. There is no contention in this case that MMIA's deficit is in any degree caused by MMIA's own inefficiency or other default, or that of any other insurance company.

The obvious effect of compelling MMIA to run a deficit for decades at a time—with private insurers compelled to underwrite the deficit—is to threaten MMIA's members with substantial losses, totalling many millions of dollars, while saving doctors a like sum in subsidized malpractice insurance. Although insurer-members of MMIA may seek to pass that enormous cost along to their customers, there are severe constraints on their ability to do so. Insurance is a highly competitive business, and competitive pricing will severely limit MMIA's members' ability to include the high costs of MMIA membership in the rate base of MMIA members' property, casualty, and other insurance policies.[13] Moreover, any attempt by

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[13] The competitiveness of the property and casualty insurance industry in New York and the current market condition of property and casualty insurance will make it difficult for companies to recoup through rate increases any assessment that they will be forced to pay. In 1987, for example, there were 287 companies writing property and casualty insurance in New York. *Best's Executive Data Service*, Report A2, A.M. Best Company, Inc., 1988. The leading four companies had only 25.6 percent of the insurance market, well below the 60 percent market share standard that is commonly accepted as indicating a potentially non-competitive market. The leading eight companies had only 41.6 percent of the market, again well below the 80 percent standard commonly accepted as a sign of non-competitiveness. Moreover, no single company had more than 7.4 percent of the market. *See Best's Market Share Reports*, 1988 (market share numbers); Tillinghast, Nelson

MMIA member-insurers to recoup an assessment through high rates would prompt swift entry into the market by new or established companies previously not doing business in New York. Such new or potential entrants in the New York market, able to set rates without regard to prior assessments, would prevent MMIA members from charging significantly higher rates to recoup those prior assessments.[14] And doctors may choose to self-insure or seek other risk-spreading devices rather than pay extraordinarily high rates. Competitive forces, therefore, will assure that the loss will largely be concentrated on MMIA member-insurers.[15]

Nor would the unconstitutional and unfair effect of New York's actions be ameliorated even if MMIA's members *could* spread a significant part of the burden to their customers. Such spreading would merely change the *source* of the subsidy to the doctors insured by MMIA, not the fact of state-compelled private subsidization. Any customer of one of MMIA's member companies forced to pay higher insurance premiums to offset MMIA's stag-

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& Warren, Inc., *Report to Vermont Department of Banking and Insurance*, December 4, 1986 (describing market-share standards).

[14] Because new companies will not have been subjected to the assessment, they will have a competitive advantage over existing firms in the New York insurance market. Capital and surplus requirements are low in the insurance industry, and fixed asset requirements consist primarily of home office, branch office, and computer facilities. These can be bought, leased, or rented on short notice. Of course, for existing insurance companies expanding into a new State, these entry barriers would be even lower since they already possess home office and computer facilities.

[15] If the Superintendent were to declare MMIA insolvent, claims of MMIA's insureds would become the responsibility of the Property/Casualty Insurance Security Fund, which is in turn funded through assessments of all property and casualty insurers writing policies in New York. N.Y. Ins. Law § 7603 (McKinney 1985 and Supp. 1989). The Superintendent thus has the authority to compel all property and casualty insurers in the State to make good on the underfunded commitments MMIA is presently required to make.

gering losses would be subsidizing the doctors entitled to purchase malpractice insurance at MMIA's subsolvency rates. Mandating this subsidy of MMIA's customers by customers of MMIA's member companies is not fairer than requiring the member-insurers to bear the burden alone.

Just such an unfair compelled private subsidy underlies the "future surcharge" approach taken by the Superintendent and the Court of Appeals: even if the Superintendent *does* approve the future surcharge, the costs of medical malpractice policies for doctors *currently* insured will merely be shifted unfairly to *future* doctors. Current and future doctors are *not* identical; doctors enter practice, leave practice, change States, change insurers, and, in some cases, choose to self-insure.

Moreover, competitive conditions will almost certainly doom the planned "recoupment" through a future surcharge precisely because requiring this subsidy of present doctors by future doctors *is* unfair. The premise of New York's decision to compel MMIA to write insurance at below cost has been that rates that would have permitted MMIA to break even would have also "discourag[ed] physicians and dentists from initiating or continuing their practice in New York." Medical Malpractice Reform Act of 1986 (L 1986, ch 266), Section 1, quoted in *MMIA v. Sup't*, Cert. Petition, App. C., at 18a. A dramatic rise in MMIA's rates in the nineteen nineties—to surcharge-enhanced levels of up to twenty-five percent above an "adequate" rate—would surely create as much discouragement as would the at-cost rates rejected by the State in 1985. Rates twenty-five percent above rates adequate to offset future losses would certainly induce many doctors who would otherwise purchase malpractice insurance through MMIA instead to self-insure or to seek alternative risk-spreading devices. Desertion of MMIA by its customers would prevent MMIA from *ever* recouping the losses New York is presently imposing on

it, even if the Superintendent *did* elect to authorize a high surcharge.

If the holding of the Court of Appeals is permitted to stand, it will have a particularly adverse impact upon the medical malpractice insurance industry nationwide. By the end of 1987, thirteen medical malpractice JUAs, including New York's MMIA, had been created by twelve States and Puerto Rico, *see* NCC Study at 1, and all thirteen *required* private insurers to be members of the association as a prerequisite to writing insurance in the State. *See generally* NCC Study. Five of the thirteen JUAs had a market share in 1987 above 45% of the market for malpractice insurance in their particular States. NCC Study at 31.[16] Four of the five were operating at a deficit at the close of 1987, the most recent year for which authoritative data are available.[17]

Eleven medical malpractice JUA States permit or require assessment of insurers in the event the JUA operates at a deficit and is unable to pay claims against it.[18]

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[16] The market shares of certain medical malpractice JUAs for 1987 were as follows: Florida, 10.4%; Kansas, 5.9%; Massachusetts, 84.5%; Minnesota, 0.4%; New Hampshire, 52.5%; New York (MMIA), 14.3%; Pennsylvania, 3.4%; Rhode Island, 75.1%; South Carolina, 53.7%; Texas 9.9%; Virginia, 2.8%; Wisconsin, 46.8%. NCC Study at 31.

[17] The deficits for these four JUAs, after taking into consideration investment income, were estimated as follows: Massachusetts, $430,000,000; New Hampshire, $700,000; Rhode Island, $74,000,000; and South Carolina, $4,800,000. NCC Study at i. MMIA's $244,800,000 discounted deficit as of the end of 1987 was among the very highest in the Nation, *see id.*, despite its relatively small share of New York's market. Although some might argue that tort reform and other developments may have moderated the level of certain of these deficits, New York's assertion of the power to impose such deficits virtually at will threatens reescalation of such debt at any time.

[18] Texas has already assessed insurers for the deficit of its joint underwriting association. NCC Study at i. Texas assessed insurers in 1985 and 1986. *Id.* at 24.

Id. at 1. If the decision below is allowed to stand, nothing will prevent all ten of the other States from shifting the costs of medical malpractice insurance to members of their JUAs just as New York has done. Insurance companies impressed as "members" of those JUAs would then be compelled to underwrite truly eye-popping deficits. *See* n. 16, *supra*. The ruling permits state legislatures to underprice privately-written insurance as a political solution to the high cost of medical malpractice. Indeed, if the decision of the Court of Appeals is not reversed, nothing will prevent the remaining forty States from adopting a similarly "convenient" solution to medical malpractice and fiscal problems of their own without recourse to increased spending and higher taxes.

The Court of Appeals' decision could also affect types of insurance other than medical malpractice. Many similar plans or insurance pools in other casualty insurance areas—such as automobile insurance [19] and workers' compensation [20]—are generating deficits in many States. And New York's compelled-private-subsidy mechanism could be employed even outside the field of insurance, requiring public utilities or petroleum companies, for example, to subsidize their customers over extended periods of time.

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[19] Automobile Insurance Plans Service Office, AIPSO Facts 1987/1988: A Handbook of Auto Shared Market Facts and Figures at 8. Of the more than 127 million passenger cars insured in the United States, 7.8 million receive insurance through shared market mechanisms. *Id.* at 12. Every State has a shared market mechanism, and 42 jurisdictions have automobile insurance plans. *Id.* at 8. The plans of several States are generating large deficits. *See, e.g., An Evaluation of the Massachusetts Automobile Insurance Market, With Recommendations for Change*, Prepared for the American Insurance Association by Goldstein & Manello (Nov. 1988) (Massachusetts); N.Y. Times, Aug. 7, 1988, at 33 (New Jersey).

[20] Reinsurance pools for workers' compensation have been created in 41 States. The National Council on Compensation Insurance, Management Summary for 1987 on Workers Compensation Reinsurance Pools at 11 ("NCCI Study").

CONCLUSION

This Court must review the Court of Appeals' extraordinary assertion of state power to confiscate and redistribute property.

Respectfully submitted,

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